

Northeast Supply Chain Conference

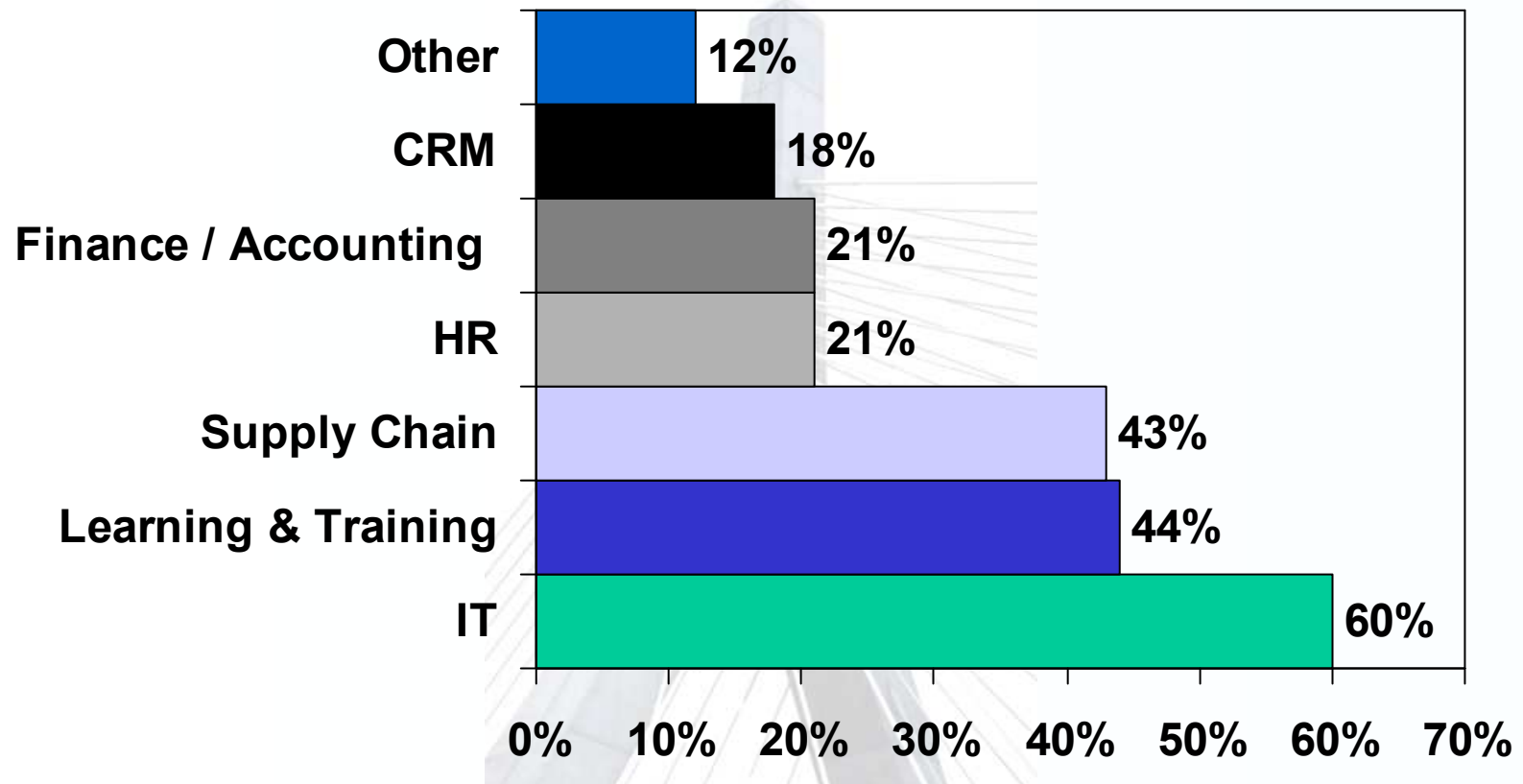
Avoiding the Pitfalls of Outsourcing

**How to insure the success of your
outsourcing efforts**

Panel Members

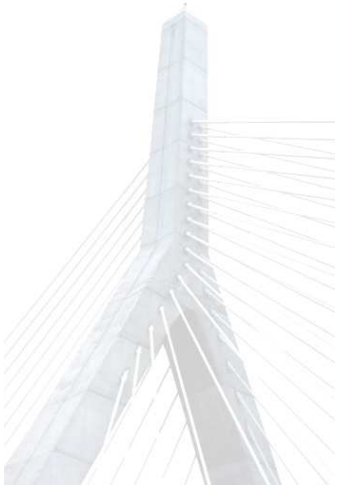
- **Karen Fedele C.P.M.**
 - Category Manager, Global Procurement, Gillette Corporation
- **Terry Hendrix**
 - Director, HP Managed Services Business, Process Outsourcing, Software Publishing Services
- **Thomas Noonan, CPIM**
 - Purchasing Manager, Textron Systems

Focus Areas for Outsourcing



Outsourcing Challenges

- **Successful Supply Chain Characteristics**
 - *Agility, Adaptability, Alignment*
- **Suppliers who ‘don’t get it’**
- **Mismanaged supply chains cost \$\$\$**
 - Over \$10 billion a year in cost management issues
 - Inventory imbalance , expedite issues, quality costs, customers satisfaction problems
- **What can we learn from the experiences of other companies?**



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Karen Fedele C.P.M.

Lack of Clearly Defined Goals and Objectives

Symptoms	Mitigating Techniques
<ul style="list-style-type: none">▪ Project begins with decision made regardless of due diligence findings▪ Focus is on financial savings only▪ Unresolved issues and differences	<ul style="list-style-type: none">▪ Expand goals beyond cost savings: transformation, innovation and shared risk/reward▪ Balance shareholder needs and resolve differences▪ Align Client / Service Provider goals<ul style="list-style-type: none">• Client: costs ↓, service quality ↑• SP: revenue ↑, delivery costs ↓

Project goals and objectives govern the outsourcing decision-making process

Project Fit and Scope Assessment

Symptoms

- SOW no clearly stated
- Economies of scale not considered
- Fuzzy scope
- Incomplete scope
- Pre-determined decision to outsource or pre-selected Service Provider

Mitigating Techniques

- Define SOW and SLA at project onset
- Clearly articulate long-term strategy for outsourced services
- Incorporate “Dragnet” clauses into the agreement
- Strive for widest practical scale – global if possible
- Keep an open mind

Breaking a large-scale outsourcing project into smaller gates will enable you to clearly define the project and scope

Start small, expand when stable

Flying Solo

Symptoms

- Under-staffed, under-resourced project team
- Failure to recognize lack of expertise with outsourcing agreements
- Confidential nature of the project limits access to internal resources

Mitigating Techniques

- Engage sourcing advisors
- Retail legal counsel with specific experience in outsourcing service agreements
- Assemble cross-functional team to assist on as as needed basis: HR, Legal, Treasury, Finance, IT, Risk Management, Medical, Security

To ensure project success, assemble a core team of dedicated resources with one person solely responsible for the project's deliverables

Draw on additional resources when necessary

Sales Puffery

Symptoms

- Capabilities are overstated or non-existent
- New technologies and processes are “in beta” or “under development”
- Blame it on the client
- It’s “proprietary and confidential”

Mitigating Techniques

- Site visit to view what’s available in production
- Live demonstrations of proposed technologies and processes – no canned presentations, screen shots or simulations
- Client references

**Avoid basing your decision on future capabilities
Decide what’s needed today and make your service
provider selection accordingly**

Ignoring Termination Issues

Symptoms

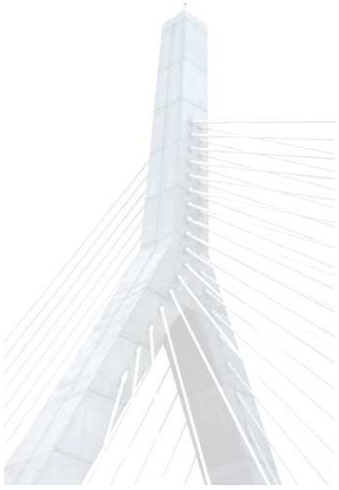
- **Contract contains no provisions for termination – natural or otherwise**
- **Reluctance to “sour” the relationship at the beginning by talking about what happens in the end**
- **Mindset that outsourcing agreement is “forever”**

Mitigating Techniques

- **Address various termination scenarios in contract**
 - Cause
 - Convenience
 - Contract End Date
 - Change in Control
 - Bankruptcy/Insolvency
- **Build in access to resources and technology during transition period**

All contracts must end at some point in time

Complexities associated with outsourcing agreements require you to incorporate exit strategies in the contract



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Terry Hendrix

Why Outsource?

(which ones are good reasons?)

- **Reduce Costs (usual reason)**
- **Better/Faster Product or Service**
- **Source of Innovation**
- **Refocus Freed Resources to Higher Value Work**
- **Assistance to Expand Market**
- **Everybody is doing it**
- **Senior Management Told Us to Outsource**

How Do You Know a Contract Is Failing?

- **25 – 50% Outsourcing Contracts Fail!!**
- **Outsourcers Expectations Not Met:**
 - Costs higher than expected
 - Service levels (time/quality) not being met
 - No continuous improvement
- **Vendors Expectations Not Met:**
 - Profit margins are lower than expected
 - Customer dissatisfied
 - Employees unhappy

What are Some Causes of the Problems?

- **Poor Preparation**
- **Outsource for the Wrong Reasons**
 - Imitate competition
 - Cover deeper problems
- **Outsourcer/Vendor Culture Incongruent**
- **Too Many Eggs in One Basket** (too complex for one vendor)



Some Guidelines for a Successful Outsourcing Contract

■ Prepare

- Determine strategic and tactical goals
- Determine what should be outsourced
- Determine the total costs
- Determine key metrics for success
- Determine the benefits of outsourcing
- Determine the risks
- Begin change management process/communications

Some Guidelines for a Successful Outsourcing Contract (cont'd)

- **Ensure Vendor is Capable (maybe one is not enough to meet your goals)**
- **Ensure Vendor Culture Meshes with Yours (it could be a long relationship!)**
- **Develop a Flexible Service Level Agreement with a Balanced Scorecard (change happens and the vendor needs a realistic set of metrics – so do you)**
- **Develop a Governance Model and Team**
- **Implement a Change Management and Communications Plan**

Some Guidelines for Evaluating/Selecting a Vendor

- **Check references and ask the references for other references**
- **Contact a customer who has left the vendor**
- **Interview and agree on your prime contact/delivery manager from the vendor**
 - Do the personalities mesh??
 - Qualifications
- **Check the vendor's financial position**
- **Is this a core competency or a new business for the vendor?**
- **What are the vendor certifications? ISO9000, Balderidge, etc.**
- **Check to see if vendor is outsourcing part of the work.**

Introduction to Governance

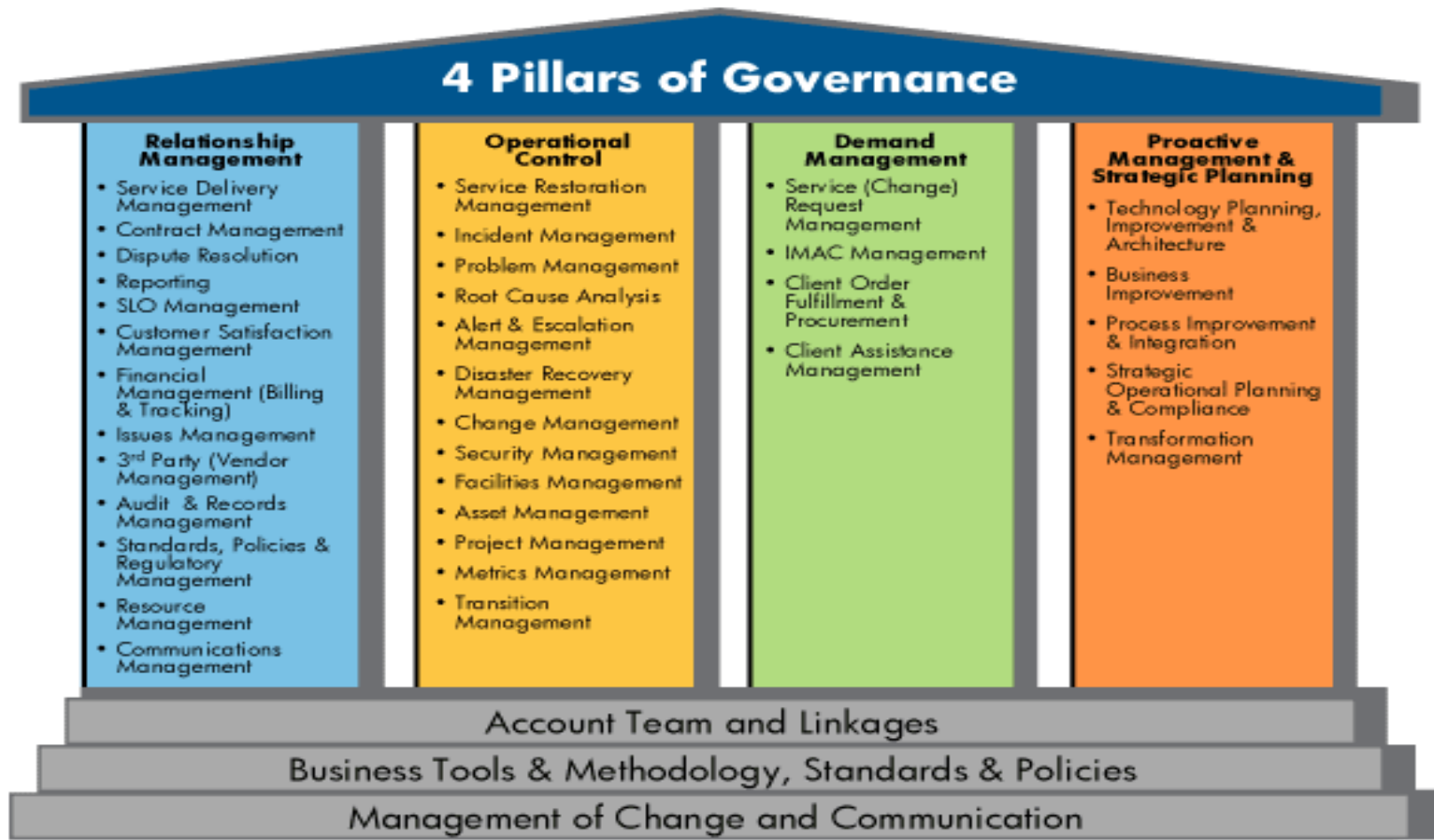
What is it?

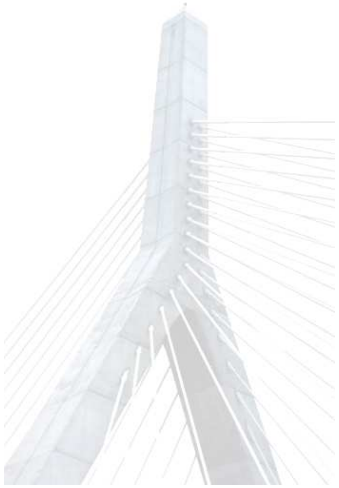
Governance is a formal framework & structure supported by a set of standard, documented processes & best practices, which enable the outsourcer and customer to mutually manage their relationship, expectations, contractual dependencies and services. Governance is dependent on the scope and breadth of the contract and the willingness of the parties to engage. It allows the outsourcer to fulfil its contractual obligations and create a successful customer experience.

Why is it needed?

It defines the parameters of the emerging partnership and details the standard processes & linkages for communicating, executing the contract and delivering goods and/or services. Effective governance is a cornerstone to credibility that leads to increased trust, stronger relationships and business growth.

Example of a Governance Model





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Thomas Noonan CPIM

Outsourcing from a Providers Perspective

- **Third party provider view of the “Good” and “Bad’ aspects of the process**
- **Major OEM’s and Smaller companies make the same mistakes**
- **Communications and ‘assumptions’ lead to the majority of issues**
- **Two examples.....**

The Good!

Situation

- **Partnership between a major iron supplier and major manufacturing services supplier**
- **Enjoyed World Class metrics in a dynamic environment**
 - Unlimited permutations of products
 - Orders immediately acknowledged upon receipt – customer received a ship date that was achieved at a 99% accuracy level.
 - Although schedules very dynamic, suppliers on time delivery equally high – although not 99% in all cases, in high 90s
- **Quality product arrived on time at customer destination with iron supplier's badge while EMS supplier's involvement "almost" invisible!**

The Good!

What made it good?

- **Service level documentation understood by all relevant parties, particularly front line folks from both organizations – rules commonly understood**
- **Key players from both organizations understood and utilized by both partners**
 - Knowing the “right people” facilitated problem solving particularly at the “ground troop” level.
 - Knowing how to contact the “right people”, while basic, was available and updated regularly by both partners
- **Communication was regular and organized**
 - Brief (10 minutes or less) con calls at individual contributor level by relevant individual contributors
 - Monthly reviews contained minimal surprises and focused on mutual improvements, non-adversarial

The Good!

What made it good?

- **Assigned staff in both organizations competent and skilled – no “throw-ins”**
- **Systems**
 - Compatible – no org to org conflicts
 - Mature – capabilities fully understood and exercised
 - Skilled users – able to push the limits of the applications’ possibilities from both users and IT support.
 - Reliable
- **Resulted in a mutually profitable, mutually satisfying relationship for years.**

The Bad!

Situation

- **Partnership between a major iron supplier and major manufacturing services supplier**
- **Suffered through a series of missed deadlines, milestones, and opportunities.**
- **Front line relationship became increasingly adversarial and non-productive**
- **Critical product launch missed**
- **Disappointment ruled the relationship from both perspectives**

The Bad!

What made it Ugly?

- **Confusion reigned. Service level agreement unclear, vague, subject to interpretation and misunderstood.**
- **Key players changed frequently.**
- **Systems not completely compatible. Data exchange frequently incomplete and/or unsuccessful.**
- **Outsourcing partner facility reeling from a major IT event – learning curve – bad timing**

The Bad!

What made it Ugly?

- **Customer partner – racing the clock, accelerating deadlines, “breaking in” a new supplier partner on a volatile program**
 - Design changing
 - Sourcing strategy frantic
- **Supplier partner – breaking in a new team with a new customer**
 - Insufficient resources
 - “Inefficient resources” – new to company, processes, etc
- **Net result wrong team handling the wrong product at the wrong time!**

Preventing The 'Ugly' in a Partnership

- **Clearly communicate expectations – both partners**
- **Choose the correct partner**
 - Understand the pricing paradox - what appears to be the lowest cost , may not be so , based on 'assumptions'
- **Clarify all aspects of expectations**
- **Establish complete reviews of all stages of the process**
 - Milestones, project management

Preventing The 'Ugly' in a Partnership

- **Don't underestimate the amount of “sweat equity” that must be invested to make the partnership work by both partner teams**
 - Get to know each other's “players”
 - Minimize turnover
 - Learn the rhythms and establish a routine
 - Insure compatibility of systems
- **Measure, Measure, Measure!!! Insure performance meets or exceeds expectations through regular reviews – both partners must step up!**

Rules for Outsourcing Success

- **Measure for success in the partnership: Measure critical outcomes of the relationship.**
- **Select a supplier who will partner with your company to provide for total 'value add' in the relationship**
- **Focus on the relationship. Contracts provide the basis for the performance but manage all aspects of the relationship for guaranteed success.**
- **Share rewards from the relationship. Provide incentives for improved performance from your suppliers.**
- **Actively manage the relationship. Insure that all parties are involved in regular communications on performance , issues, and objectives of the outsourcing efforts.**
- **Pay attention to detail: Focus on objectives, costs, and quality performance. Make sure that partners know exactly what is expected of them in each of these areas.**

Avoiding the Pitfalls of Outsourcing

Thank you for your participation in today's Panel discussion

